CBI MARKET SURVEY

The software and IT services market for offshore and nearshore outsourcing in the UK

Publication date: December 2007

Report summary

This CBI market survey discusses, among other things, the following highlights for the software and IT services market for offshore and nearshore outsourcing in the United Kingdom (UK):

- Estimated at €46 billion, the UK is the largest IT market in the EU, ranking ahead of Germany, France and Italy.
- The software and IT services market will keep on growing.
- The UK software market is dominated by four large companies (IBM, Microsoft, SAP and Oracle). They account for 39% of the market.
- The UK is the largest offshoring market for IT in the European Union (EU).
- The sectors with the best potential for offshoring / nearshoring for SMEs from DCs are financial companies, local government bodies, manufacturing companies and medium sized insurance companies.
- India is by far the largest outsourcing destination for the UK.

This survey provides exporters of software and IT services with sector-specific market information related to gaining access to the UK. By focusing on a specific country, this survey provides additional information, complementary to the more general information and data provided in the CBI market survey 'The software and IT services market for offshore and nearshore outsourcing in the EU', which covers the EU market in general. That survey also contains an overview and explanation of the selected services dealt with, some general remarks on the statistics used, as well as information on other available documents for this sector. It can be downloaded from http://www.cbi.eu/marketinfo.

1   Market description: demand and supply

There is a clear relationship between Section 1 and 2 of this survey. Section one, below, will provide information on the end market for software and IT services in the UK. The structure and growth of this end market determine the opportunities for offshore / nearshore outsourcing, which will be the topic of Section 2.

Demand

Estimated at €46 billion, the UK is the largest IT market in the EU, ranking ahead of Germany, France and Italy. The UK also has the highest per capita spending on IT in Europe. Looking forward, there is growing optimism in the market, caused by factors which include continuing public sector spending on major IT procurements, and the recently awarded 2012 Olympic Games.

The UK is facing a potentially critical shortage of technology professionals. The IT industry is growing at five to eight times the national average, and around 150,000 entrants to the IT workforce are required each year. At the same time, every year fewer young people choose to study technology-related subjects at school and university; and every year fewer technology graduates choose a career in IT. There are many initiatives taken by the UK government with the aim to increase interest in technical studies.

The second quarter of 2007 was the best for IT job-seekers in several years, with double-digit growth in the full-time and freelance job markets. The number of permanently advertised jobs increased by 13% compared to the same period in 2006, and there were 18% more contract positions on offer, according to the Computer Weekly Survey of Appointments Data and Trends compiled by Salary Services Limited (SSL).

Software

The market for software products in the UK valued €16.8 billion in 2006 (Table 1.1). This was a 7.4% increase compared to 2004. The software market will continue to record significant growth (see Table 1.1) and is forecast to grow to €18 billion in 2008.

Table 1.1   UK software market in € million, 2004 – 2008

	2004	2005	2006	2007*	2008*
Systems software	7,311	7,961	8,597	9,320	10,076
Application software	6,286	6,696	7,039	7,467	7,907

* forecast
Source: EITO (2007)

Systems software

As security remains one of the top priorities of Chief Information Officers (CIOs) in the UK, system infrastructure software will record double-digit growth. Software piracy is a major issue for the computer software market. The focus of software spending is on system infrastructure, with demand driven by system management, network management, storage software and security software. Another area that is growing is the market for virtualisation software that makes it possible to use different systems more flexibly. Applications tools, especially segments of information management software are expected to grow significantly more than the other segments because of a growing demand to make better use of the information available within a company.

Application software

The application software market will also see a sustained growth, thanks to higher demand in content, collaborative, Enterprise Resource Management (ERM), and Customer Relationship Management (CRM) application software. The current focus on Business Intelligence, an information access and delivery solution, ensured positive developments in the area of application development in 2006 and is also expected to do so in 2007.

Sectors

The most important growth drivers for development of software in the UK are the public sector, banking and insurance and the manufacturing sector. Manufacturing companies are looking to improve efficiency in their business processes and have renewed interest in Enterprise Resource Planning (ERP) applications. Industry-specific applications are a key priority in the financial services and healthcare sectors in particular.

IT services.

The current focus on Business Intelligence displayed by UK enterprises ensures positive developments in the area of application deployment for both 2006 and 2007. The IT services market in 2006 valued €31 billion and is forecast to grow to €34 billion in 2008.

Table 1.2   UK IT services market in € million, 2004- 2008

	2004	2005	2006	2007*	2008*
Professional services	19,728	21,261	22,544	23,831	25,068
Support services	7,580	8,076	8,520	8,970	9,433

* forecast
Source: EITO (2007)

Professional services

Demand is high in the area of professional IT services in the UK. According to a recent survey conducted in Northern Ireland on custom made software applications, professional services come second with regard to demand.

Support services
In the permanent IT jobs market, it is the rise in demand for PC support staff that is most notable, as this has been a relatively depressed area for several years. Jobs advertisements here were up by nearly 50% in 2006.

Supply

Software
The UK software market is dominated by four large companies (IBM, Microsoft, SAP and Oracle), that account for 39% of the market. The next 20 competitors account for 16% of the market. There are five indigenous suppliers (Misys, Sage, iSoft, Northgate and RM) in the UK top 10. The major vendors have substantial presence in the UK and cover most areas of the market. Opportunities exist for niche players or those with strong vertical applications.

Recent trends show that there many mergers and acquisitions of UK companies with or by other companies from the EU, especially France. It is the focus on profitability that results in this supplier consolidation. A recent example is the acquisition of 'Xansa plc' by the French company 'Groupe Steria SCA'. The main reason for these acquisitions is the effort to increase profitability but an additional aim is to enter new supply markets like India. Many UK based companies have staff in offshoring locations, primarily in India, which makes them interesting for other EU companies. Struggling to maintain prices on the same level also results in new offers, such as low cost services after buying the software. For an overview of the UK's leading software providers please refer to Table 1.3 below.

Table 1.3   Leading software providers on the UK market

Company	Internet
BMC Software Ltd	http://www.bmc.com/en
Computer Associates PLC	http://www.ca.com/gb
Hewlett-Packard Ltd	http://www.hp.com/country/uk/en
IBM United Kingdom Ltd	http://www.ibm.com/uk
Microsoft Ltd	http://www.microsoft.com/en/gb
Oracle Corporation UK	http://www.oracle.com/global/uk
The Sage Group PLC	http://www.sage.com
SAP (UK) Ltd	http://www.sap.com/uk
SAS Institute	http://www.sas.com
Symantec (UK) Ltd	http://www.symantec.com/en/uk

Source: Facts Figures Future (2007)

IT services
Similar to the software sector, the main market trends on the UK IT services market are cost reduction and mergers and acquisitions (For example 'Logica CMG' that acquires 'Unilog'). Profitability in the segment of IT services is not very high and there is a strong pressure by the management of the companies to find a way to increase profitability. For an overview of the leading IT service providers in the UK please refer to Table 1.4.

Table 1.4   Leading IT service providers on the UK market

Company	Internet
Accenture	http://www.accenture.com/Countries/UK
Atos Origin	http://www.uk.atosorigin.com
BT Group PLC	http://www.btplc.com
Capgemini UK PLC	http://www.uk.capgemini.com
Computer Sciences UK Ltd	http://uk.country.csc.com
Electronic Data Systems Ltd	http://www.eds.com
Fujitsu Services Holdings PLC	http://www.fujitsu.com/uk
Hewlett-Packard Ltd	http://www.hp.com/country/uk/en
IBM United Kingdom Ltd	http://www.ibm.com/uk
LogicaCMG	http://www.logicacmg.com

Source: Facts Figures Future (2007)

Technology regions
The most important technology clusters in software and IT services in the UK are 'Silicon Glen', and 'The Cambridge network'.

Silicon Glen
The name, Silicon Glen -http://www.siliconglen.com - is applied to the Central Belt triangle between Dundee, Inverclyde, and Edinburgh, and includes Fife, Glasgow and Stirling. Many hi-tech companies are established in Silicon Glen, including Sun Microsystems, Motorola, Agilent, IBM, Microsoft, Raytheon, Oracle Corporation, Cadence Design Systems, 3Com, Adobe Systems, Semefab, Brand Rex, BI Technologies, CRC Group, Compugraphics, National Semiconductor, Micronas and Atos Origin.

The Cambridge Network
The Cambridge Network - http://www.cambridgenetwork.co.uk - is a networking organisation for business people and academics working in technology fields in the Cambridge area (sometimes called Silicon Fen). With over 1,000 corporate and 300 individual members it supports Europe's largest and most vibrant venture-funded technology cluster (often referred to as the Cambridge Phenomenon).

Trends
- The UK IT industry faces a shortage in skilled employees.
- Business intelligence analytical tools and CRM software are showing an increasing demand in the UK market.
- According to different market forecasts, the outsourcing market for both software and IT services will continue to grow in the UK in the coming years, but with a decreasing growth rate.
- Open source software is gaining in importance and it is expected that a large part of the server market will turn to Linux in the near future.
- The overall focus of the UK IT services market is on the intelligent delivery of services, the use of fewer call centres and the move to outsource more non-core support services.
- Acquisition of UK companies by companies from other countries in the EU is a noticeable trend caused by EU consolidation in order to increase competitiveness.

Opportunities and threats
+ The UK is the largest market for outsourcing, offshoring and nearshoring in the EU and can therefore offer good opportunities for DCs.
+ Decreasing popularity of the IT profession in the UK could increase the chances for offshore/nearshore providers.
+ CRM and business intelligence software developers have increasing opportunities because of an increasing demand for these services in the UK market.
+ The market for outsourcing (onshore / offshore / nearshore) of software and IT services is forecast to keep on growing in the near future, which offers chances for DC suppliers.
− The use of more open source software can be a threat to suppliers from DCs that want to offer their services in the UK market.
− As UK companies are bought by companies from other EU countries to increase competitiveness, it might be more difficult for DC suppliers to operate in the EU market.

Useful sources
- Association of Independent Computer Specialists - http://www.aics.org.uk
- British Computer Society - http://www.bcs.org.uk
- Business link - http://www.businesslink.gov.uk
- Information Technology Telecommunications and Electronics Association - http://www.intellectuk.org - Click on 'Improving markets', than on 'Outsourcing and Offshore Group' and finally on 'Outsourcing & Offshore Group Charter' in order to download a list of UK based companies that could be potential offshore partners for companies in DCs.

- Missions Economique - http://www.missioneco.org - for information on software and IT sectors EU-wide, click the country, then 'sector industrielle' and finally "electronique et NTIC". Information is in French.
- UK trade & invest - https://www.uktradeinvest.gov.uk

2 Offshore outsourcing

Where section one of this survey focused on the market for software and IT services in the UK in general, this section will zoom in specifically on the market software and IT services offshoring and nearshoring in the UK as this is the market with the best potential for SMEs from DC.

The market
Although already rather mature, the UK market will remain the most dynamic and advanced outsourcing market in Europe, with companies struggling with issues like cost control, increasing business demand (especially in large enterprises) and short return on investments.

According to Forrester Research –a worldwide technology and market research agency-, the UK will account for more than 75% of the €3.5 billion western European expenditure on offshore outsourcing of IT services by 2009. The UK is expected to remain the largest European market for offshoring of IT services, with India being the main destination.

Offshoring activities within the software sector in the UK are expected to increase from €4.5 billion in 2000 to almost €13 billion in 2008 according to RNCOS (market research agency). An increase in software development skills in DCs has accelerated the pace of this offshoring trend. UK companies will double offshore IT staff numbers by 2008, according to analyst 'Ovum'.

One of the new offshoring activities in the UK is offshoring of Software as a service (SaaS). SaaS is a software application delivery model where a software vendor develops a web-native software application and hosts and operates (either independently or through a third-party) the application for use by its customers over the Internet. Customers do not pay for owning the software itself but rather for using it. Although offshoring in this segment is still not widely spread in the EU, the UK begins to use offshoring of SaaS and it is ranked second after the US in this area. An example of a company that uses SaaS offshoring is Salesforce.com - http://www.salesforce.com

Chances for offshoring/nearshoring
From the point of view of technical expertise chances for offshoring/nearshoring are generally high for both software development and IT services because of a workforce shortage in the UK. On the other hand, chances for development of end applications in vertical markets also depend on good knowledge of particular segments of the targeted vertical market and not only on technical skills.

Applications software
Application software offers the best chances for both nearshoring and offshoring. Application development, CRM and Enterprise Content Management (ECM) are the most popular services for outsourcing, especially for medium-sized and large companies in the financial sector. Although application software is primarily represented in the financial sector, the manufacturing sector is more suitable for SMEs from DCs. The reason for this is that production companies use offshore services from companies of all sizes while the banking and insurance sector usually cooperate with larger suppliers of these services. Offshoring of more critical business components like ERP is still not very popular because companies still consider offshoring / nearshoring of this segment as potentially risky and rely on onshore outsourcing.

Systems software
In the systems software segment chances for offshoring / nearshoring are somewhat smaller than in application software. Nearshoring destinations are slightly more popular because communication is a more vital factor for these kind of complex IT projects. Geographical proximity and a the small time difference also play a role

Professional IT services
Chances for nearshoring and offshoring of Professional IT services are not so high because of very heavy competition of UK based consultancy companies.

Support software
Certain support services, such as remote management and helpdesk, could be offshored / nearshored. The main issues for this service are cost reduction and language proficiency.

Reasons and barriers to offshoring/nearshoring
According to a survey conducted by the Confederation of British Industry, the main reason for offshoring / nearshoring in knowledge intensive business sectors like the IT sector is cost reduction. Another important reason is the shortage of IT professionals in the UK. Other reasons are process improvements, proximity to new customers and focus on core business.

Critical success factors
Business communication, a clear offer, ability to cut prises and reliability of the supplier are the most important success factors for nearshoring / offshoring in the UK. Furthermore, the skills and knowledge level of the outsourcing staff are very important. There is a growing demand for SAP technical skills. According to "Salary Services Limited" the top 5 skills on the UK IT market are: SQL, C, Office, Java and SQL server. Demand for all of the skills mentioned is expected to increase in 2007 compared to 2006.

Sectors
The best sectors for outsourcing for SMEs from DCs in the UK are the financial sector, local government bodies, the manufacturing sector and medium-sized insurance companies as they attempt to contain costs and transform their infrastructure. The local governmental sector (for example healthcare) also uses outsourcing services because of the shortage of resources in the local market.

Important offshore/nearshore destinations for the UK
Still the most important offshore destination for software and IT services is India. Market analysts agree that in the future there could be a shift from India to China. Work that, until recently, would have been offshored to India is already moving to China. In the present situation China is used as offshoring destination, not directly by UK companies but by Indian companies that offshore work to Chinese companies. According to a survey conducted by TPI research, India is used as an offshoring destination for IT services by 75% of the survey respondents, but there is close competition for the second place between Central and Eastern Europe (28%) and China (25%). The leading Indian offshoring companies in the UK market are 'Wipro Technologies', 'Infosys' and 'Tata Consultancy Services'. Sri Lanka is also a popular offshoring destination because of the low cost labour force and easy access to a large talent pool. Another important offshoring destination is South Africa. Latin American countries are still not widely used as offshoring destinations for UK IT companies.

The important nearshore destinations for the UK are Central European countries such as Romania, the Czech Republic and Poland. Also Ireland is a very competitive nearshore destination because of the very small cultural differences with the UK.

Trends
- Fear of job loss is increasing in the UK labour market.
- Shortage of IT professionals in the UK.

- The leading Indian players continue to rapidly increase their market share in the UK software and IT services market.
- There is increasing pressure from the side of UK companies to reduce costs, which requires more innovative solutions from suppliers in order to keep a stable price level.
- According to market analysts, at least one offshore-based player will appear in the top ten UK IT companies by the end of the decade.
- Standardisation of IT services is a growing trend in the UK.

Opportunities and threats

+ The shortage of IT professionals in the UK could provide opportunities to SMEs in DCs by means of outsourcing.
+ SMEs in the UK do not have the resources to pay teams of programmers £100 an hour. This provides opportunities to SMEs from DCs that have much lower wages.
± The public sector could be suitable for offshore and nearshore DC companies as local governments search for low cost providers. In order to establish cooperation with the public sector, it is preferable to have a partnership with local providers.
± As a result of standardisation, providers of niche services from DCs will have more trouble selling their services in the UK. Providers of standardised services however, have better chances in the UK market.
− A very strong presence of large Indian offshore players could pose a threat to offshore / nearshore services of SMEs from other DCs.

Useful sources

- IntellectUK – http://www.intellectUK.org - UK trade association for software and IT services
- National outsourcing association (NOA) - http://www.noa.co.uk
- Offshoring blog – http://www.offshoringblog.net - A website with articles about offshoring.
- ZD net - http://www.zdnet.co.uk - Articles of offshoring in UK.

3   Trade structure

In this paragraph, the general distribution channel for software and IT-services will be discussed. These channels apply to each EU-market and, therefore, also to the UK market.

The most important channels for software related services are:
1. Establishing your own sales office.
2. Consultant/broker.
3. Partnership with UK (software) company.
4. Direct contact with a UK software manufacturer.
5. UK software manufacturer setting up his own factory in a developing country.

The most important channels for IT services are:
1. Establishing your own sales office.
2. Consultant/broker.
3. Partnerships with large service providers (system integrators) in the UK.
4. Contacting end-user organisations directly.
5. Contacting local offices of multinationals in the home country of the services provider.

Names of some main players and their websites can be found in Section 1. For more information about the trade structure for outsourcing software related services, please refer to the CBI market survey "The software and IT services market for offshore and nearshore outsourcing in the EU".

Entry strategy

For the SMEs from DCs a good advice is not to look at the UK as one market but to explore differences among the regions. For the first step, one of the most useful sources could be regional governmental bodies. To find information about possibilities for entering the market in

different regions in the UK and for potential partners please have a look at the website of the UK governmental organization 'UK Trade & Investment' - https://www.uktradeinvest.gov.uk.

Also in the UK, the best way to enter the market is via an intermediary such as a consultant or a broker, to set up your own sales office, or to find a partner in the UK.

Some examples of companies that act as intermediaries in the UK software and IT services market are:
- Cognite - http://www.cognite.co.uk
- Onshore offshore - http://www.on-off.co.uk
- Overpass - http://www.overpass.co.uk
- Quickstart global - http://www.quickstartglobal.com

Specific trade structure facts for UK
- The public sector buying process is still formal and at times long-winded. There are often too many suppliers invited to compete, which leads to low profit rates and high bidding costs. However, this is changing, largely as a result of pressure from the UK industry body IntellectUK.

Useful sources
- Euroitx - http://www.euroitx.com
- IntellectUK – http://www.intellectUK.org - UK trade association for software and IT services.
- UK Trade & Investment - https://www.uktradeinvest.gov.uk.

4   Prices and margins

According to Salary Expert (http://www.salaryexpert.com), a software engineer working in the UK now earns an average annual salary of between €51,000 and €52,000. When benefits and bonuses are added to this salary, the average total compensation for this position would be between €53,000 and €54,000. Table 4.1 shows average costs for an IT services company per person in the UK compared to the average costs for an employee in a DC.

Table 4.1   Comparison of offshoring costs, € per hour

	UK company	Typical offshore company
Average daily cost of employment per person	179	126
Daily cost of desk space	36	Included
Daily cost of computer/IT communication services	10	Included
Other employee benefits	14	Included
Management costs	23	Included
Total costs	**262**	**126**

Source: Watson, 2006

Useful sources
- Distributors, agents and other distribution channels.
- IntellectUK – http://www.intellectUK.org - UK trade association for software and IT services.
- Trade press or trade fairs
- UK Trade & Investment - https://www.uktradeinvest.gov.uk
- Websites of competitors.

For more information please refer to the CBI market survey "The software and IT services market for offshore and nearshore outsourcing in the EU".

5   Market access requirements

As a service provider in a DC preparing to access UK, you should be aware of the market access requirements of your trading partners and the UK government.

Requirements are demanded through legislation and through labels, codes and management systems. These requirements are based on working conditions, health and safety and social concerns. You need to comply with EU legislation and have to be aware of the additional non-legislative requirements that your trading partners in the EU might request.

For information on legislative and non-legislative requirements, go to 'Search CBI database' at http://www.cbi.eu/marketinfo, select ITO and UK in the category search, click on the search button and click on market access requirements.

6   Doing business

General information on doing business, like approaching potential business partners, building up a relationship, drawing up an offer, handling the contract (methods of payment, and terms of delivery) can be found in CBI's export manuals 'Export Planner' and 'Your image builder'. Furthermore, cultural awareness is a critical skill in securing success as an exporter. Information on cultural differences in the EU can be found in Section 3 of CBI's export manual 'Exporting to the EU'. The CBI manuals can be downloaded from http://www.cbi.eu/marketinfo - go to search publications.

Sales promotion
Software and IT services can be promoted through several sources. Below some of the most important trade press and trade fairs can be found.

Trade press
The following UK magazines are specifically focussed on Software and IT services:
- Computer Weekly – http://www.computerweekly.com
- Computing - http://www.computing.co.uk
- Infomatics - http://www.infomaticsonline.co.uk
- ITWeek - http://www.itweek.co.uk
- Silicon - http://www.silicon.com
- ZDNET - http://www.zdnet.co.uk

Trade fair
An excellent promotion tool is participating in a major trade fair in Europe. Exhibiting at a fair is not only an effective opportunity to promote your company and services, it is also an effective instrument for benchmarking with your competitors. The most important trade fairs for software and IT services in the UK are:
- Online Information - http://www.online-information.co.uk - Annually, December, London - The world's leading event for online content and information management solutions.
- Outsource World London - http://www.outsource-world.com/london - Annually, April, London - Largest outsourcing exhibition in UK.
- Storage expo - http://www.storage-expo.com - Annually, October, London – UK data storage event.

Others
These days, it is an absolute must to have a professional website, which is aimed at your main target groups. Make it interactive and promote it in the proper way. More information can be found in the CBI Export Manual 'Website Promotion', available at http://www.cbi.eu/marketinfo. Furthermore, participating in conventions or congresses may also be a promotional tool.

<center>This survey was compiled for CBI by Facts Figures Future.
Disclaimer CBI market information tools: http://www.cbi.eu/disclaimer</center>